SUPREME COURT, U. S.
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No. ~~1426~~

In the
Supreme Court of the United States

OCTOBER TERM, 1967

HAROLD Z. KAPLAN, Shareholder in, suing derivatively for and on behalf of all shareholders for the benefit of: ONE WILLIAM STREET FUND, INC., a Maryland corporation, ENERGY FUND INC., a Delaware corporation, THE DOMINICK FUND, INC., a Delaware corporation, CHEMICAL FUND, INC., a Delaware corporation; and HAROLD Z. KAPLAN and FREDERICK L. DUNN, DANIEL B. DUNN, CHARLOTTE F. DUNN and NANCY L. DUNN, Minors, by next friend and parent, LILA DUNN, Shareholders in, suing derivatively for and on behalf of all shareholders for the benefit of: THE LEHMAN CORPORATION, a Delaware corporation,

Petitioners,

vs.

LEHMAN BROTHERS, a partnership; GOODBODY & CO., a partnership; DOMINICK & DOMINICK, INCORPORATED, a corporation; UNKNOWN MEMBER ORGANIZATIONS OF THE NEW YORK STOCK EXCHANGE TRANSACTING BROKERAGE BUSINESS FOR CHEMICAL FUND, INC. and other Defendant-Funds; PAINE, WEBBER, JACKSON & CURTIS, a PARTNERSHIP; THE NEW YORK STOCK EXCHANGE, ONE WILLIAM STREET FUND, INC., a Maryland corporation; ENERGY FUND INC., a Delaware corporation; THE DOMINICK FUND, INC., a Delaware corporation; CHEMICAL FUND, INC., a Delaware corporation,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The petitioners respectfully pray that a writ of certiorari issue to the United States Court of Appeals for the Seventh Circuit to review the judgment of that Court entered on

January 4, 1967, which affirmed the order of the United States District Court for the Northern District of Illinois, Eastern Division granting respondents' motion for summary judgment.

OPINIONS BELOW

The opinion of the Court of Appeals for the Seventh Circuit is reported in 371 F. 2d 409. It is printed in the Appendix attached to this petition at p. 10a. The opinion of the District Court is reported in 250 F. Supp. 562 and is also printed in the Appendix at p. 1a.

JURISDICTION

The judgment of the Court of Appeals was entered January 4, 1967 and is hereinafter set forth at p. 12a. No rehearing was sought by petitioners. The time for filing a petition for certiorari was extended to May 26, 1967 by orders of Mr. Justice Clark entered on April 4, 1967, May 4 and 22, 1967.

The jurisdiction of this Court is invoked under Title 28 U. S. C. § 1254 (1).

QUESTIONS PRESENTED

1. Whether the adoption and enforcement of an agreement by the New York Stock Exchange and its members to charge brokerage commissions on the basis of uniform, minimum rates, and their adherence to such rates under coercive Exchange sanctions, is immunized by the Securities Exchange Act of 1934 (15 U.S.C. §78 *et seq)* from the operation of Section 1 of the Sherman Act (15 U.S.C. § 1) declaring agreements in restraint of trade illegal?

2. Whether the Securities Exchange Act of 1934, the self-regulatory scheme it established allowing registered exchanges to fix reasonable rates of commission, and the scheme of regulatory oversight assigned to the Securities and Exchange Commission over reasonable rates of commission by § 19 (b) of that Act impliedly repealed the operation of the antitrust laws to the agreement of the New York Stock Exchange and its members fixing uniform minimum rates of commission, although said agreement was never approved by the Commission or found by it to be in furtherance of the Act's reasonable rate standard or its substantive aims and purposes to protect investors?

3. Does the self-regulatory scheme created by the Securities Exchange Act of 1934 permit respondents to adopt a uniform, minimum rate fixing agreement so as to impliedly repeal the antitrust laws irrespective of whether such agreement is economically unjustifiable, results in unreasonable and unconscionable profits, discriminates against large institutional traders, artificially inhibits members from offering competitive rates contrary to their willingness and ability to do so, and so operates as to corrupt fiduciary duties and produce large scale conflicts of interest between mutual funds, their investment advisers and Exchange brokers?

4. Is the Securities Exchange Act of 1934 scheme of S.E.C. regulatory oversight over rates so pervasive as to impliedly repeal the antitrust laws' application to respondents' uniform, minimum rate-fixing agreement, nothwithstanding the fact that the S.E.C. never held a rate hearing, never issued a rate order, never compiled a rate record, never made a rate finding and never defined the Act's standard of reasonable rates or articulated the criteria applicable to such definition?

5. Is respondents' rate fixing agreement exempt from the antitrust laws when New York Stock Exchange members themselves subvert the fixed rate concept by handling institutional brokerage business (almost 50% of public round-lot trading) at 30% to 40% of fixed rates, but their uniform commission rate agreement prohibits the "saving" from accruing back to the institutional traders?

6. Under the standard of "reasonable rates of commission" as set forth in Section 19 (b) of the Securities Exchange Act of 1934, does the New York Stock Exchange and its members have the right to legislate their own antitrust immunity by merely adopting uniform, minimum rates in conflict with the antitrust laws and filing same with the S.E.C., and if such self-legislated immunity requires no affirmative S.E.C. approval, is not such self-regulatory power an unconstitutional delegation of legislative power to a non-governmental, private business group?

7. Where investors have no effective remedy permitting them to trade on the New York Stock Exchange at reasonable rates or to recover damages for unreasonable rate overcharges except under the antitrust laws, is it not imperative to preserve such remedy?

STATUTES INVOLVED

The statutes which the case involves are:

1. Section 1 of the Sherman Anti-Trust Act (15 U.S.C. § 1);
2. Sections 4 and 16 of the Clayton Act (15 U.S.C. § § 15 and 26); and
3. Sections 2, 6 (b) and (d), 15A as amended, and 19 (b) of the Securities Exchange Act of 1934 (15 U.S.C. § § 78b, 78 f (b) and (d), 78 o—3(b) (8) and 78 s (b).

The full text of these statutes insofar as here pertinent is set forth in the appendix to this petition, *infra*, pages 12a-17a.

The Securities Exchange Act of 1934 is hereinafter referred to as "the 1934 Act" or "the Exchange Act" and the Sherman and Clayton Acts are referred to as "the antitrust laws."

STATEMENT OF THE CASE

This action was brought pursuant to 15 U.S.C. § 15 by petitioners derivatively on behalf of five large mutual funds against the New York Stock Exchange (hereafter, "NYSE") and five of its member firms to recover treble damages sustained by reason of respondents' agreement fixing uniform minimum rates of brokerage commission and their adherence to and enforcement of same in violation of the Sherman Antitrust Act, 15 U.S.C. § 1 (A. 3-35).[1] Other relief of a declaratory and injunctive nature was also sought, the effect of which would restrain the NYSE from interfering with the rights of individual NYSE members to set their own competitive minimum rates of commission (A. 29).

In response to the Amended Complaint respondents filed a motion for summary judgment with a supporting affidavit (A. 36-65). Plaintiffs filed a Counteraffidavit[2] and subsequently, sought to file a cross motion for summary

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[1] All reference to (A.—) are to petitioners' appendix filed in the court below and references to (App.—) are to the appendix attached to this petition.

[2] Because of the size of the Counteraffidavit the Clerk of the Court below did not bind it up with other parts of the record or assign record page numbers to it. Reference to the Counteraffidavit is made to its own page numbers, abbreviated herein i.e. (Counteraffidavit, 27) or to an exhibit therein, i.e. Counteraffidavit Exhibit 7.)

judgment together with a Supplemental Affidavit.[3] The trial court denied petitioners' leave to file said motion and Supplemental Affidavit and also denied petitioners' application to file the Supplemental Affidavit in opposition to respondents' motion. The trial court entered summary judgment for the respondents (A. 80-89), which order was affirmed on appeal by the Court below (App. 12a). Hereinafter set forth are relevant matters herein as developed by the pleadings and affidavits.

The mutual funds on whose behalf this suit was brought by petitioners are engaged in the business of investment of the funds of their stockholders. A major portion of this investing is in stocks of the corporations listed and traded on the NYSE. The purchase and sale (collectively trading) of said stocks is transacted primarily through the facilities of the NYSE through members brokers. Such trading is subject to NYSE commission law (A. 45-52).

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[3] The Court below granted petitioners leave to file their Supplemental Affidavit as part of the record although leave to file said document was denied by the District Court. The sole references made hereto to matters contained in the Supplemental Affidavit are to public documents incorporated therein comprising public statements and correspondence of S.E.C. Chairman Cohn. The sources of these utterances are identified in the Supplemental Affidavit.

The Court below excused printing of petitioners' Counteraffidavit and Supplemental Affidavit as well as a separately bound Appendix of Exhibits. Petitioners also filed in the District Court sundry exhibits denominated "Source Exhibits" consisting of the five part Record of Special Study of Securities Markets of the Securities Exchange Commission, House Document No. 95, 88th Congress, 1st. Sess. The New York Stock Exchange Fact Book 1965 and the NYSE Annual Report, 1965. The Securities and Exchange Commission Special Study in hereinafter referred to as the Special Study. Printing of said source exhibits was also excused.

The NYSE is an unincorporated association owned by its members. Its sole object as set forth in its Constitution is to furnish facilities for the transaction of member business, to maintain high standards of commercial honor and integrity and to promote just and equitable principles of trade. The Exchange itself carries on no commercial activity, and its Constitution declares no economic aim or purpose for itself or its members. The government of the Exchange is vested in its Board of Governors. The Board has authority to prescribe rules, but provisions in the Constitution (including those relating to its rate fixing law) can only be adopted or altered by majority vote of the total membership. (A. 20-21)

The NYSE is the nation's primary trading market. About 90% of the dollar trading in all NYSE listed shares traded on all exchanges is traded on the NYSE. And, of the remaining 10%, NYSE members, as dual members of regional exchanges, trade upwards of 60%. (Counteraff. 3). NYSE members, in 1964, dominated the government of virtually all important regional stock exchanges as well as the National Association of Securities Dealers, Inc. (the only association of over-the-counter brokers registered with the S.E.C.) (A. 27). NYSE members also dominated trading volume in the over-the-counter market where NYSE minimum rates are the prevailing brokerage rates. The minimum rates prevailing on the NYSE are and have been the rates adopted by regional stock exchanges, with respect to NYSE listed issues. In summary, NYSE members transact over 90% of all brokerage business in stocks in the United States.

"The avowed objectives of organizing the NYSE, in 1792, were the setting of minimum commission rates and the establishment of a preference for members of the Exchange in their dealings with other members * * *." Special Study, Part 2, p. 295. In furtherance of these objectives,

the Constitution of the Exchange, adopted by the membership, contains provisions governing every phase of membership, access to the Exchange market, and the charging of commissions. These provisions are collectively referred to as "commission law"[4] and provide, among other things, that commissions shall be charged and collected at rates not less than prescribed rates and shall be net and free from any rebate, return, discount or allowance made in any manner or by any method of arrangement, direct or indirect (A. 34). Other key provisions of commission law perfect and uphold the objective sought by the minimum rate concept, as follows:

First, only members can trade on the NYSE, and its Constitution limits membership to 1,366 natural persons (an increase of only 266 members since the year 1879) thus establishing a monopoly market. (Counteraff. 21-23). The limitation on the number and availability of memberships, together with the enormous increase of trading volume on the Exchange in the last three years, has resulted in the rising price of a seat which reflects the value of trading access to the Exchange at fixed non-competitive rates[5] (NYSE Annual Report, 1966, p. 24).

Second, a major structural characteristic of commission law is the charging of the same commission rate, based

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[4] Relevant portions of commission law are set forth in the Amended Complaint (A. 31-34).

[5] One effect of the premium price of a seat is to exclude membership of thousands of registered professional securities dealers who are unable to afford a seat. An antitrust action raising this point is now pending against the NYSE alleging that its commission law effects a concerted exclusion of all non-member brokers from participation in profitable intercourse (via shared commissions) on business referred to Exchange members for execution on the Exchange. *Thill Securities Corp.* v. *the New York Stock Exchange,* 63 C 264 (E.D. Wis.)

on the value of the round lot (100 shares), for each transaction regardless of size.[6] The commission on an order for 5,000 shares is exactly fifty times that of an order for 100 shares.[7] Volume traders that buy or sell in blocks of 1,000 shares or more, e. g. mutual funds represented by petitioners and other institutional investors, are allowed no discount or rebate whatever (Counteraff. 50).

Third, a major advantage of membership in the Exchange is in the preferential brokerage rates accorded to members on their own trading as principals for their own account (Supp. Aff. 187). A member trading 100 shares of stock at a market price of $40.00 per share pays a commission of only $7.70 at NYSE "internal rates" compared to the non-member rate of $39 ($7.70 of which goes to cover the same internal services). This internal commission is paid to other NYSE members for floor brokerage (actual execution of the transaction) and clearance (exchange of cash, certificates and bookkeeping). An institutional investor placing an order for 5,000 shares directly with a floor-broker (and by-passing the commission house) is required, by commission law, to pay

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[6] Commission law prescribes a separate schedule of rates applied to trades of odd-lots (less than 100 shares). Such trades are handled on the floor of the Exchange by two odd lot dealers who share a duopoly in such trading. In addition to the NYSE prescribed rates, these dealers add on a charge of their own, called the "odd lot differential." The NYSE and the odd-lot dealers are presently defendants in an antitrust suit alleging an antitrust conspiracy in fixing the rate of the "odd-lot differential." *Eisen* v. *Carlisle & Jacquelin, et al,* 66 C. 1265 (S.D. NY.)

[7] As noted in the reply of an institutional trader to a questionnaire prepared by the Special Study, Part 2, p. 320: "It costs little, if any more, to execute single trades of 5,000 or 10,000 shares than it does for 1,000 or 100 shares."

the full $39 rate per hundred shares to the floor broker. The funds represented by petitioners are not qualified under the NYSE Constitution to be member corporations of the Exchange. As a consequence, mutual funds, along with other institutions trading on the NYSE must trade through Exchange members at commission rates that provide no relief from NYSE prescribed schedules adopted to the 100 share unit of trading. Indeed, commission law prohibits members from even making a proposition for the transaction of business at less than minimum prescribed rates (A. 34).

Fourth, before a member is allowed trading privileges he must sign a written pledge to abide by the Constitution, as amended from time to time, and all rules adopted pursuant thereto. In addition, all allied members of the Exchange (all partners of members, or holders of voting stock in member corporations) must sign such pledge. (A. 32). A member or allied member adjudged guilty of violating the constitution of the Exchange may be suspended or expelled by the Board of Governors (A. 32). The Exchange has punished members violating commission law (A. 39).

All of the aforementioned provisions were in force when on September 11, 1934, the NYSE filed its application for registration as a national securities exchange under the 1934 Act (A. 39). The application incorporated the Constitution of the Exchange (A. 39). Seventeen days after such filing the S.E.C. entered an order registering the Exchange (A. 53). There is no record of any proceeding in connection with the order granting registration, and the S.E.C. does not regard the order of registration an opinion of the S.E.C. (Appendix of Exhibits, Ex. 39). The order of registration itself noted the limitations of time to consider the evidence supporting the application

(A. 53). In view of the fact that the Exchange Act makes it unlawful to trade on an exchange unless it is registered, a delay would have had the effect of closing the NYSE.[8]

As noted, commission law is adopted by the Exchange membership on a one-man, one-vote basis. But, the Exchange membership is essentially split into two camps. The majority of NYSE members are what is known as floor professionals (stock specialists, independent floor brokers, odd-lot dealers and their associate odd-lot brokers, and floor traders). (Counteraff. 26). These floor professionals have little or no direct contact with the investing public. A minority number of the memberships in the Exchange are held by persons engaged in the public brokerage business. Although twenty-five member organizations in the NYSE receive almost 50% of all commissions arising from public trading, these firms contain only 7% of the members of the Exchange. NYSE members and member organizations accounting for only 10% of all commissions hold 60%. of the memberships. (Counteraff. 29). In 1961, Merrill, Lynch, Pierce, Fenner and Smith, Inc., the Exchange's largest brokerage organization, accounted for 13% of all commissions on the NYSE, but it contained only 11 members, .81% of the total (Counteraff. Ex. 4).

Since 1934, the Exchange membership has voted on only two aspects of commission law, rate increases and the allowance of discounts to large traders. The NYSE membership vote on the last four out of five rate increases was as follows:

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[8] Page 1 of the Application for Registration stated in part, "* * * this application for registration is made solely in order to avoid penalties imposed upon an exchange by said act." New York Stock Exchange, by Richard Whitney, President.

Year of Rate Increase	*Yes*	*No*	*Percentage Voting Against Increase*
1938	523	413	44%
1942	779	206	21%
1953	639	530	45%
1958	646	593[9]	48%

Voting is by secret ballot, making it impossible to reconstruct an economic relationship (re: the amount of commissions attributable to each vote) between those voting for or against the increase. The S.E.C. never polled members to determine if those voting against the increase in fact accounted for more commission business than members voting for the increase (Counteraff. 31 & Ex. 8).

Only once in the 175 year history of the Exchange (in 1953) has the issue of a discount been put to a member vote. Notwithstanding the recommendation of the majority of a NYSE special committee urging adoption of discounts, the Exchange membership defeated the proposal by a vote of 573 to 532, 48% of the votes being in favor of the discount (Counteraff. 65).

[9] Merrill Lynch filed a minority report vigorously opposing the 1958 rate increase proposal (Appendix of Exhibits, Ex. 36). Commission law compelled it to adopt the increase with resultant enormous profits (Counteraff. 49).

Each increase raise approved by the Exchange membership was recommended on the basis of studies and formal reports of a special committee of the Exchange (A. 40). Copies of such rate raises, as approved, were furnished the S.E.C. as required by the 1934 Act (A. 40). Respondents' affidavit attached to their motion for summary judgment sought to establish that each rate raise was reviewed and analyzed by the S.E.C. which thereafter did not object (A. 40-44).[10] However it appears that the S.E.C. has never "held public hearings on * * * commission rates and it has never exercised its powers under Section 19 (b) to alter or supplement the Exchange's rules relating to commission rates" (Appendix of Exhibits, Ex. 40). Nor is there any norm or criteria by which the reasonableness of such rates could be ascertained. (Counteraff. 40; Special Study, Pt. 2, p. 343).

The ineffectiveness of S.E.C. review of Exchange rates is shown by the Special study is as follows (Counteraff. 39, 40);

a) "Since the enactment of the Exchange Act in 1934, the NYSE has amended its non-member commission rate

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[10] Respondents' affidavit is conspicuous for what it fails to allege. It does not allege, for example, that the NYSE ever filed a report with the S.E.C. justifying uniform rates or no-discounts or reciprocal gives-ups or that commission law and practice was reasonable; nor did any report ever define reasonable rates or rate structures or specify any particular percentage or range of percentage or profit in relation to the 1934 Act's standard of reasonable rates. Similarly, the affidavit did not allege any facts with respect to its own rate review during the 25-odd year period when the five rate increases were adopted. Insofar as commission law prohibits the allowance of discounts but permits reciprocal give-ups of commission and that these matters are part and parcel of minimum rate commission structure, the affidavit is totally silent.

five times. Each of the increases was recommended by a special committee of the Exchange in a formal report which became the basis of the Exchange's proposal." (Special Study, Pt. 2, p. 329)

b) "The underlying data used by the Commission in reviewing each rate change have essentially been those which the NYSE has supplied at the time of its proposal * * * (except for 1942). The data supplied by the Exchange has been limited by the scope of its samples and the contents of its report forms." (Special Study, Pt. 2, p. 342).

c) "In no instance has any particular percentage or change has been limited by the scope of its samples and Exchange or the Commission in relation to Section 19b's reasonable standard or the concept of 'fair return' as used by the 1942, 1947 and 1958 Exchange committees (and possibly others)." (Special Study, Pt. 2; 337).

(d) "The significant point is that, despite the Exchange's numerous references to a profit percentage and its several mentions of 'fair return' as seemingly the ultimate criteria of 'reasonable rates,' there seems never to have been any clear articulation of the significance of the amount or percentage of profits, or of any other quantitative standard, as a measure of a fair return or of the reasonableness of a particular rate schedule." (Special Study Pt. 2, 337).

(e) "Neither the Commission nor the Exchange has articulated what principles apply in relating the profit percentage to return on capital, when the former is the sole or primary element remaining to be measured or whether other elements are encompassed." (Special Study Pt. 2; 336).

(f) "Nor is it clear, assuming that the profit percentage is deemed to have broader coverage than return on capital, exactly what relationship it is thought to bear to the general statutory standard of reasonableness, i.e., whether any particular percentage of profit is indicative of the reasonableness or unreasonableness of any particular level of rates." (*ibid.*)

The Decision Below

The court below affirmed the judgment of the trial court which was interpreted "as holding that the antitrust laws are inapplicable to the New York Stock Exchange insofar as its prescribing of minimum commission rates is concerned" (App. 11a). The affirmance appears to be based upon the following:

a. *Silver* v. *New York Stock Exchange*, 373 U. S. 341 (1963) stands for the proposition that although the 1934 Act contains no express exemption from the antitrust laws, a repeal thereof is to be regarded as implied if necessary to make that Act work (App. 11a);

b. Section 19 (b) of the 1934 Act authorizes the S.E.C. to alter or supplement rules of exchanges with respect to such matters, among others, as the fixing of reasonable rates of commission (App. 10a);

c. The fixing of uniform minimum commission rates is an exercise of the Exchange's self-regulatory function under Section 19 (b) because the fixing of such rates is one method of regulating commission rates (App. 11a);[11]

[11] Of course, no one could deny this oversimplification. However, it is completely irrelevant to this case since the self-regulatory function of the Exchange under Section 19(b) is not to fix *just any rates* but to fix *reasonable rates* which under that Section must be those which

d. The antitrust laws and the 1934 Act cannot be construed as showing a congressional intention to permit an antitrust suit based on the Exchange's agreement relating to rates of commission charged by its members (App. 11a).[12]

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[11] (Continued)

"are necessary or appropriate for the protection of investors." The aims of the 1934 Act in this regard, referred to in thirty-six sections of the Act, as noted by Judge Clark in *Baird* v. *Franklin*, 141 F. 2d 238, 244 (2nd Cir. 1944), were completely ignored both in the Court below and the trial court.

Nor does the Court below indicate why uniform minimum rates are necessary to make the 1934 Act work, thus making its reliance on *Silver, supra* irrelevant also.

[12] The basis and authority for this statement remain undisclosed by the court below.

REASONS FOR GRANTING THE WRIT

I.

THERE IS AN URGENT NEED TO CLARIFY THE APPLICABILITY OF THE ANTITRUST LAWS TO THE EXCHANGE ACT'S STANDARD OF REASONABLE RATES AND THE ACT'S SCHEME OF EXCHANGE SELF-REGULATION AND S.E.C. REGULATION.

A. The Effect of the Decision Below Frustrates The 1934 Act's Objectives to Protect Investors.

The case at bar presents to this Court for the first time the important issue of whether the agreement of the NYSE and its members which fixes minimum rates of brokerage commission is vulnerable to the antitrust laws as a restraint of trade or is impliedly exempted therefrom by the 1934 Act. Necessarily comprised therein is the issue of the applicability of the antitrust laws to enforce a substantive standard of the 1934 Act, *i.e.* "reasonable rates of commission" (15 U.S.C. § 78 s (b) (9), in the light of the primary and basic aims and purposes of the Act to protect investors.

These issues were adversely decided against investors in the court below which found such an implied exemption upon a misapplication of *Silver* v. *New York Stock Exchange*, 373 U.S. 341 (1963) and upon a misconstruction of congressional intent in the enactment of the 1934 Act. The basis for its decision, that the Exchange may fix minimum rates of commission because the 1934 Act permits it to fix reasonable rates in order to make the Act work, is illogical; it ignores the starting premise of the 1934 Act that rates be reasonable in order to protect in-

vestors.[13] As a result the NYSE and its members, under the guise of self-regulation, are permitted to perpetuate a rate-fixing scheme in restraint of trade which solely rewards their own self-interest and which lacks any redeeming

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[13] Petitioners are aware that it is not the office of a petition for certiorari to fully argue the merits of the questions presented. However, in support of the above statement, it is pointed out that *Silver*, pp. 361-363 emphasized substantive fulfillment of the aims and purposes of the 1934 Act before antitrust immunity could be implied as to any activity of the Exchange. It stands for proposition that where NYSE collective action imposes an antitrust restraint which frustrates rather than furthers the 1934 Act's aims and purposes, the application of the antitrust laws to the restraint does not create any conflict between the two statutory schemes. Instead, the antitrust laws are to be regarded as "peculiarly appropriate as a check upon anticompetitive acts of exchanges which conflict with their duty to keep their operations and those of their members honest and viable." And "denial of their applicability would defeat the congressional policy reflected in the antitrust laws without serving the policy of the Securities Exchange Act." (*Silver*, p. 360)

The court below did not apply these principles but disposed of the issues on the narrow, unevaluated and simplistic approach that fixed minimum rates are nothing more than permissible self-regulation under the 1934 Act. Such an approach is totally divorced from the Act's aims and purposes and their effective fulfillments to protect investors against unreasonable rates. Nothing in the record made by respondents or in the decision supports any contention that minimum rates are necessary to make the 1934 Act work.

On fundamentals there is complete harmony between the 1934 Act standard of reasonable rates and antitrust laws standards of competitively reasonable rates (via its prohibition of rate-fixing agreements). Both achieve a similar goal, protection of the public against unreasonable rates. An application of the antitrust laws to respondent's rate fixing agreement rather than conflicting with the 1934 Act's standards, serves to implement and fulfill it.

virtue of furthering any aim or purpose of the 1934 Act to protect investors. Respondents did not attempt in the record here to make any showing that its fixed minimum rates do further such aims.

It is true, of course, that after such rates are fixed the S.E.C. is authorized to alter or supplement them pursuant to the standards of Section 19 (b) of the 1934 Act. The decision below, however, was not supported by any recognition of such powers of oversight in the S.E.C. as bearing on the question of implied repeal. Even if it had there are nevertheless serious questions here as to the pervasiveness of such oversight insofar as it bears upon the reasonableness of fixed rates. This is pointed out by the S.E.C. in its discussion on this subject in its Special Study, Part 2, p. 343 as follows:

> "The statute (Exchange Act) imposes the general standard of reasonableness without further definition. It is the kind of general standard that needs to be given consent in the course of administration; yet after nearly 30 years there has been no comprehensive and consistent public articulation on the part of the Exchange or the Commission, of the principles or criteria to be applied in interpreting the standard."

As of May, 1967, neither the Exchange nor the S.E.C. has yet defined what reasonable rates are, or identified what criteria are applicable to a definition. The scheme of self-regulation and S.E.C. regulation may be discussed and debated *ad infinitum,* but the fact remains that without a starting definition of reasonable rates (and applicable rate criteria) there never could be and never has been responsible, legitimate, justified, good faith or arguably lawful compliance or even attempted compliance with the standard. Without a definition, the standard itself is meaningless. The combined failure of the Exchange and

the S.E.C. to define the standard constitutes the most complete breakdown and failure of a regulatory scheme in the annals of American administrative law.

Reasonable rates either mean "something" or the statutory standard is a nullity. The consequence of a meaningless standard is the denial of protection the standard is supposed to provide. Rates and rate structure are economic stuff, and the only meaningful and workable hypothesis of reasonable rates is economic reasonableness. Section 2 of the 1934 Act itself recites no competitive or economic policy whatever, nor does it contain any special or protective policy which might conflict with the concept of economic reasonableness. Moreover, the Exchange Act does not empower exchanges or the S.E.C. to innovate economic policy. Reasonable rates of commission are the sole rate standard and the immediate frame of reference. Cf. *McLean Trucking Co.* v. *United States,* 321 U.S. 67, 79-80 (1944). There is no more persuasive evidence of the purpose of a statute than the words by which Congress undertook to give expression to its wishes. *United States* v. *American Trucking Ass'ns.,* 310 U.S. 534, 543 (1940).

B. The Interests of a Great Segment of the National Economy is Adversely Affected by the Decision Below.

At the current trading volume the investing public is currently now paying over $1.2 billion annually for the privilege of trading on the NYSE at uniform fixed minimum rates. About 35-40% of this amount is being paid by institutional investors (including banks administering private trusts), without the benefit of discounts.[14] Mutual

[14] Facts in the record, based on statistical data available through 1965, show that institutional trading comprised approximately 40% of total public (non-member) trading on the NYSE. At the Investment Bankers Association

funds alone are paying about $100 million annually to trade on the Exchange, and a substantial portion of these commissions are, as a result of the prohibitions against discounts or rebates, diverted into reciprocal give-ups.

Over twelve million persons own shares listed on the NYSE and over three million persons own shares in mutual funds. These investors, both institutional and otherwise, ought to be able to trade on the NYSE at reasonable rates and rate structure. They constitute a huge segment of the national economy. Obviously the decision below must have serious impact on them, emphasizing the importance of the resolution by this Court of the questions here presented, particularly insofar as institutional investors are concerned. In this connection, it is pointed out that between 1949 and 1964 the holdings of NYSE listed stocks by financial institutions went from $9.7 billion to $97.7 billion, percentagewise from 12.7% to 20.6%. If one includes NYSE listed stock held in personal trusts administered by banks at year-end 1963, out of a total of $411 billion value in all NYSE listed stocks, institutions and bank trusts held approximately $150 billion. In 1963, institutions accounted for 23.9% of total share volume, but this figure is about 30% of public volume (at full commission rates), since total volume comprises members' own trading (about 20% of the total). In 1965, institutions accounted for 31.4% of total shares traded, or

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[14] (Continued)
55th Annual Convention, in November, 1966, S.E.C. Chairman Cohen stated: "We estimate that currently about one-half of the total public commission income of NYSE members of round-lot transactions is attributable to transactions by institutions."

about 39% of public volume. In the 1966 NYSE study,[15] institutions accounted for 34.8% of the total dollar volume of shares traded, compared to 38.4% by individuals (non-members). Of the total dollar volume of shares traded by non-members, institutional volume in 1966 was approximately 45%.

In 1963, institutional investors paid at least $210 million in commissions on their trading on the NYSE, at uniform minimum, no-discount rates. In 1965 mutual funds alone paid over $100 million in commissions,[16] the major portion of which (70 to 80%) arose from trading on the NYSE. This sum reflects the striking growth of NYSE trading volume in the last few years, from $47.3 billion in 1962 (as cited in *Silver*), to $73.2 billion in 1965[17] and $98.6 billion in 1966.[18]

The resolution of the questions presented here is of further importance to institutional investors since the uniform, fixed rates of the Exchange affect them in two unique respects. First, such rates provide no graduated discount for the larger transactions in which the institutions tend to deal,[19] and, second, they are based on a cost structure which includes the cost of services other than the basic brokerage function—ancillary services of little or no interest or value to institutional investors. The

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[15] NYSE 14th Public Transaction Study, as related in Investment Dealers Digest, March 20, 1967, pp. 6 and 66.

[16] Source: Report of the S.E.C. on the Public Policy Implications of Investment Company Growth published December 2, 1966, cited *infra* as S.E.C. Report.

[17] Source: NYSE Fact Book, 1966, published by the NYSE in April, 1966.

[18] Source: Statistical Bulletin of the S.E.C., March, 1967, p. 10.

[19] In terms of trading patterns, a NYSE study in 1963 revealed that blocks of 1,000 shares or more made up 46.4% of all shares traded by institutions and intermediaries, compared to 32.6% in 1960.

effect of fixed rates charges institutional investors for unwanted ancillary services and deprives them of trading on the Exchange, using only the essential services required to effect transactions, and not having to pay for anything else.

As noted in the Special Study, Part 2, page 311: the question comes down to whether a commission rate favoring the volume buyer or seller might be justified by savings to the member in brokerage, sales, back office promotion or other expenses. The mechanics, time and back office expense of executing a 5,000 share trade are substantially the same as a 100 share trade. Minimum, no-discount rates simply exact from institutional traders fifty salesmen commissions, fifty units of partners compensation and fifty profit units.

The failure of the Exchange's Commission Law to provide for graduated discounts has given rise to another evil which the S.E.C. is apparently powerless to correct. This evil from the standpoint of institutional shareholders, arises from the unjustified profitability in handling institutional brokerage business in blocks. As a result, NYSE member brokers are willing to and do handle the brokerage business of mutual funds for 60-70% *below* the minimum rate schedules prescribed by the NYSE constitution. But, NYSE commission law absolutely prohibits members from rebating the "saving" back to the institutions placing the business. Commission law does, however, allow members to split commissions among one another, and does allow traders to direct the executing broker to split his commission, *i.e.* to direct what NYSE members shall receive the split and in what proportion. Under NYSE commission law, millions of dollars in brokerage fees (at NYSE rates) are directed to be split (given-up)

to ot er NYSE brokers who have performed no service to the mutual fund. This division of commissions is known as a directed split or reciprocal give-up of commissions.

The reciprocal give-up is commonly employed by the investment advisers managing mutual funds to reciprocate brokers for selling shares in the mutual fund itself. Since investment advisers are paid management fees by mutual funds based upon the asset values of the funds they manage, the sale of additional mutual fund shares increases asset value and management fees. But no benefit accrues to the fund itself or its stockholders by reason of the sale of more shares. Institutional block traders, and especially mutual funds, are thus in a position to direct vast amounts of commission business in a manner which serves the purpose suited to benefit solely the group exercising the trading power. Commission law prevents the funds themselves from benefitting from their trading power (and the willingness of NYSE brokers to execute such brokerage at less than 50% of prescribed rates) in the form of discounts of rebates.

As stated in the Special Study, Part 4, p. 234:

> "This unbalanced reciprocal structure is a direct outgrowth of a minimum rate structure which prohibits volume discounts and rebates."
>
> "Ultimately the solution of the problem lies at their source: the NYSE minimum commission rate schedule. So long as the funds cannot themselves benefit from the economies created by their mass purchasing power the complexities and potential problems of the third party beneficiary system will continue."

The problems involved in reciprocal give-ups are numerous and complex. These problems were first given

attention in the Wharton Report of 1962 and, thereafter, in the Special Study of 1963. Substantial excerpts from these reports were incorporated in petitioners' Counter-affidavit in support of the *per se* unreasonableness of fixed-rate commission law. (Counteraff. 55-62b).

On July 18, 1966, the S.E.C. staff, in a letter sent to all registered exchanges, noted that customer directed give-ups were inconsistent with the premise that fixed rates of commission were necessary or appropriate to the effective operation of the Exchange.[20]

Not until December 2, 1966, did the S.E.C. itself formally condemn give-ups and recommend their elimination.[21] That recommendation, if adopted, would simply allow NYSE brokerage firms which now give-up 60-70% of their commissions on institutional business to retain 100% of commissions. As noted in the S.E.C.'s Report, page 17: "Existing regulatory controls have neither curbed the growth of reciprocal and give-up practices nor dealt with the basic regulatory problems[22] they

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[20] This letter recommended elimination of give-ups, saying: "The directed give-up also seriously complicates the administration and assessment by the Exchanges and the Commission of the reasonableness of commission rates since commissions received and retained cease to be related to the expenses incurred for services rendered in the execution of brokerage orders * * on the Exchange." CCH, Securities Law Reporter, Number 108-117, August 10, 1966, Par. 77,360, page 82,665.

[21] Report of the S.E.C. on Public Policy Implications of Investment Company Growth, House Rep. No. 2337, Cal. No. 1046, 89th Cong., 2nd Sess.

[22] Among the problems of give-ups are the conflict of interest of a mutual fund adviser, and, especially, where such adviser, as in the case of plaintiff funds, is a member of the Exchange. While such adviser-member executes brokerage at 100% of Exchange rates, other NYSE

pose."[23] As of now, the NYSE membership has neither eliminated give-ups, nor adopted discounts, nor permitted members to effect rebates.

The denial of discounts and the use of reciprocal give-ups of commission conclusively establish the unreasonableness, arbitrariness and hypocrisy of fixed minimum rates and are therefore within the questions here presented. Under no conceivable economic, ethical, fair or equitable principles of trade as referred to in the 1934 Act can fixed rates, the denial of discounts and the use of reciprocal give-ups be deemed in compliance with the 1934 Exchange Act's reasonable rate standard.

This failure to comply affects, as earlier noted, over $1 billion a year in brokerage commission. There can be little doubt that the applicability of the antitrust laws to

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[22] (Continued)
brokers are handling other fund business at 30-40% of NYSE rates plus give-ups. And, there is also a problem of the breach of fiduciary duties of the adviser to the fund when brokerage business is placed and give-ups are directed so as to benefit the adviser rather than the fund. The use of give-ups involves NYSE brokers (and especially members who are also investment advisers) in a scheme which diverts away potential savings to the funds, and arguably violates provisions of the Investment Company Act of 1940 and the Investment Advisers Act of 1940. On January 12, 1967 the Wall Street Journal reported that ten stockholder derivative suits were filed by mutual funds alleging that the use of give-ups breached duties imposed by these Acts, and resulted in the payment of excessive brokerage fees.

[23] As noted on page 185 of the S.E.C. Report the practice of give-ups "impair the orderly and proper functioning of the securities markets themselves. * * * Give-up practices have been tolerated * * * only because brokerage costs are fixed by the *exchange minimum commission rate schedules.*" (Emphasis Supplied)

respondents' uniform rates will have the immediate consequence of competitively reducing commissions by 10-20% generally on individual trading and by 60 to 70% on institutional block trading. If such savings are to be denied to investors, such denial should rest on substantial legal grounds. The opinion below is deficient in authority or argument justifying a summary judgment on petitioners' claim. If objectives are to be balanced, how does one balance the objective of fulfilling reasonable rates via the antitrust laws and saving investors at least $200 million a year in commissions as compared to ratifying a regulatory scheme that is all shadow and no substance! The effect of the decision below affirms a regulatory illusion as a defense to an antitrust claim.

II.

THE ERRONEOUS APPROACH TAKEN BY THE COURT BELOW CONFLICTS WITH PRINCIPLES ENUNCIATED IN THIS COURT'S OPINIONS GOVERNING THE APPLICATION OF THE DOCTRINE OF AN IMPLIED REPEAL OF THE ANTITRUST LAWS. AS A RESULT OF THIS APPROACH AN ERRONEOUS DECISION HAS BEEN RENDERED, THE EFFECT OF WHICH GIVES THE NEW YORK STOCK EXCHANGE MEMBERSHIP CARTE BLANCHE TO OVERRIDE THE ANTITRUST LAWS WITHOUT ANY REQUIRED SHOWING THAT SUCH ANTITRUST CONDUCT IS LEGITIMATE, JUSTIFIED SELF-REGULATION OR THAT IT SERVES SUBSTANTIVE AIMS AND PURPOSES OF THE EXCHANGE ACT. THE DECISION PERMITS THE NYSE TO OVERRIDE THE ANTITRUST LAWS WITHOUT THE INVOLVEMENT OR APPROVAL OF THE SECURITIES EXCHANGE COMMISSION, AND RESULTS IN MAKING THE NYSE A LAW UNTO ITSELF.

Dismissal of petitioners' case preserves intact a rate-fixing agreement among NYSE members now in its 175th

year. A decision of such practical magnitude to the investing public, as heretofore shown, ought to rest on sound grounds supported by substantial authority. Instead of taking an approach which thoroughly and exhaustively examined underlying issues, especially economic issues and consequences, the court below adopted a superficial approach which did little more than summarily invoke an implied antitrust repeal. Its basis for invoking such repeal is in conflict with principles set forth in a number of opinions of this Court and requires review and reversal.

A. The Court Below Ignored Consideration of Established Principles of Law Essential To A Proper Decision In The Case At Bar.

The first principle is that the antitrust laws represent fundamental pro-competitive economic policy, and that in the absence of an immunity, the securities business like any other form of interstate trade is subject to the Sherman Act. *Silver* v. *New York Stock Exchange,* 373 U.S. 341, 360 (1963); *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 372 (1963); *Carnation Co.* v. *Pacific Westbound Conference,* 383 U.S. 213, 215 (1966); *Northern Pac. R. Co.* v. *United States,* 356 U.S. 1, 4-5 (1957); *United States* v. *Morgan,* 118 F.Supp. 621 (S.D.N.Y.).

Second, "(R)epeal of the antitrust laws by implication from a regulatory statute are strongly disfavored and have only been found in cases of plain repugnancy between the antitrust and regulatory provisions." *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 350-351 (1963); *Carnation Co.* v. *Pacific Westbound Conference,* 383 U.S. 213, 217-218 (1966). Cf. *Silver* v. *New York Stock Exchange,* 373 U.S. 341, 357 (1963); *United States* v. *Borden Co.,* 308 U.S. 188 (1939); *Georgia* v. *Pennsyl-*

vania R. Co., 324 U.S. 439, 456-457 (1945); *California* v. *Federal Power Comm'n*, 369 U.S. 482, 485 (1962).

Third, the doctrine of implied repeal will only be invoked in the context of multiple safeguards provided by a pervasive regulatory scheme. *Pan American World Airways* v. *United States*, 371 U.S. 296 (1963); *Philadelphia National Bank*, 374 U.S. 321, 350-351 (1963); *United States* v. *R.C.A.*, 358 U.S. 334, 346-350 (1959); Cf. *American Power & Light Co.* v. *S.E.C.*, 329 U.S. 133 (1941).

Fourth, when a private antitrust action for treble damages with respect to a rate fixing agreement is subject to approval by a regulatory agency, the action should be stayed rather than dismissed pending agency determination of antitrust issues, where the agency has jurisdiction over such issues. *Carnation* v. *Pacific Westbound Conference*, 383 U.S. 213 (1966). Inasmuch as the Exchange Act prescribes no mode of S.E.C. approval to defendants' rate fixing agreement and prescribes no S.E.C. jurisdiction over the antitrust issue implicit therein, the case at bar argues even more forcefully for at least a stay, rather than a dismissal, than did the *Carnation* case, *supra*.

Fifth, "(R)epeal is to be regarded as implied only if necessary to make the Securities Exchange Act work and even then only to the minimum extent necessary." *Silver*, *supra*, 373 U.S. 341, 357. Dismissal of the case at bar implied a repeal to the maximum extent, not in furtherance of the 1934 Act, but simply to exonerate respondents from treble damages.

Sixth, investor protection is a keystone of the 1934 Act. *Silver*, *supra*, 373 U.S. 341, 352-353; *J. I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1963); *Baird* v. *Franklin*, 141

F.2d 238; Loomis, *"The S.E.C. as Amicus Curiae,"* A.B.A. Journal, Vol. 52, No. 8, p. 750, (August, 1966).

Seventh, rates fixed by agreement or conspiracy are unreasonable *per se*. *United States* v. *National Association of Real Estate Boards,* 339 U.S. 485, 489 (1950); *United States* v. *Trenton Potteries,* 273 U.S. 392, 396-398 (1926); *United States* v. *Socony-Vacuum Oil Co.,* 310 U.S. 150, 218 (1940). Price-fixing schemes are also an unfair method of competition. *Federal Trade Comm'n* v. *Beech-Nut Packing Co.,* 257 U.S. 441 (1922). And the concerted denial of quantity discounts has been held to be an unreasonable restraint of trade. *Sugar Institute* v. *United States,* 297 U.S. 553, 594-595 (1936).

Eighth, a combination to fix rates, to monopolize or restrain trade through a membership device or participation in a plan or submission to a coercive device violates the Sherman Act. *Associated Press* v. *United States,* 326 U.S. 1, 19 (1945); *Interstate Circuit, Inc.* v. *United States,* 306 U.S. 208, 227 (1938); *United States* v. *Masonite Corporation,* 316 U.S. 265, 275 (1942); *United States* v.; *Paramount Pictures, Inc.,* 334 U.S. 131, 161 (1948).

Ninth, the freedom of individual business units to compete unhindered by the group action of others is one of the aims of the antitrust laws. *Silver, supra,* 373 U.S. 341, 359-360; *Fashion Originators' Guild* v. *Federal Trade Comm'n,* 312 U.S. 457 (1941); *Anderson* v. *Shipowners Ass'n.,* 272 U.S. 359, 364-365; *United Mine Workers of America* v. *Pennington,* 381 U.S. 657, 668 (1965).

Tenth, the fact that the Exchange is to some extent a regulated entity does not confer a *per se* immunity to either the Exchange or its members. *Georgia* v. *Pennsylvania R. Co.,* 324 U.S. 439, 456 (1945). The Exchange Act

was not intended to be used as a member device "to engage in predatory practices at will." Cf. *Maryland & Va. Milk Producers Ass'n* v. *United States*, 362 U.S. 458, 465-466 (1960).

Eleventh, where judicial enforcement of the antitrust laws would remove the clog of rate-fixing agreement and all the interrelated restraints embodied in commission law, such enforcement aids rather than hinders the S.E.C. in its tasks. Cf. *Georgia* v. *Pennsylvania R. Co.*, 324 U.S. 439, 460; *Silver, supra*, 373 U.S. at 359; *Pan American World Airways* v. *United States*, 371 U.S. 296, dissent, Mr. Justice Brennan, at 330.

Without a starting approach to the case at bar which recognized these starting principles, the court below could not have and did not resolve the ultimate issue pursuant to this Court's direction to invoke an implied repealer of the antitrust laws "only if necessary to make the Securities Exchange Act work, and even then only to the minimum extent necessary." *Silver, supra*, 373 U.S. at 357.

B. The Approach Adopted By the Court Below Is In Conflict With This Court's Opinion In the Silver Case, and Allows the Exchange Membership to Legislate Its Own Antitrust Immunity Via So-Called Self-Regulation Regardless Of Its Justifiableness Or Compatibility With The Aims and Purposes Of The 1934 Act.

The court below adopted an "approach" which held that since the workings of self-regulation under Section 19 (b) of the Exchange Act includes rates, and minimum commissions are one method of regulating rates, in order for the Exchange Act to "work" it is necessary to immunize minimum rates from the antitrust laws. This "ap-

proach" amounts to an absolution. It is totally divorced from the standard of reasonable rates, divorced from the substantive aims and purposes of the Exchange Act, and ignores entirely the function of the antitrust laws as "peculiarly appropriate as a check upon anticompetitive acts of exchanges." *Silver, supra,* 373 U.S. at 360. Instead of taking an approach seeking a reconciliation between the Exchange Act and antitrust schemes, the court below did not even perceive any need to attempt such reconciliation. Instead, it adopted an approach whereby exchange self-regulation is assumed to be so pervasive as to allow the exchange to legislate its own antitrust immunity by simply adopting a rate-fixing agreement in conflict with the antitrust laws and filing it with the S.E.C. This approach emphasizes self-regulation as an end in itself. Congress can hardly have been deemed to have intended to authorize exchanges to legislate their own antitrust repeal in furtherance of no more clearly delineated a standard than reasonable rates. The overtones of unconstitutionality are too grave. *Schechter* v. *United States,* 295 U.S. 495 (1935). Cf. *American Power & Light Co.* v. *S.E.C.,* 329 U.S. 90 (1946).

The *Silver* case, *supra,* at 352 noted that the Exchange Act created a federally mandated duty of self-policing and self-regulation. But the exercise of self-regulation was held not to give rise to a blanket antitrust immunity. *Silver, supra,* at 357. Before an implied immunity might arise the particular application of self-regulation had to pass muster as legitimate, justifiable and justified. *Silver, supra,* 373 U.S. at 358, 359, 361-362, 364-366. All of this was related to the fundamental proposition recognized in *Silver* that self-regulation was not an end in itself.

The obvious conflict between the opinion below and *Silver, supra,* is that the court below relieved the Ex-

change from any specific duties or tests pertaining to rate-regulation. All rates or rate structure adopted under §19(b) seemingly inherit an antitrust immunity no matter how invidious their design and intent to restrain trade, no matter how unjustified or illegitimate they are or lacking in any redeeming virtue. It would seem that Congressional benevolence in providing an antitrust dispensation of such magnitude should be supported by substantial authority, none of which was cited by the courts below.

If unjustified procedure is a basis for applying the antitrust laws, as it was in *Silver*, how much more persuasively does the case at bar argue for such application. The gravity of mischief that can be wrought in the guise of unchecked self-regulation (absent pervasive regulatory oversight) is nowhere greater than in the area of economic rate-regulation. Yet the court below adopted an approach summarily exempting respondents' rate scheme from the antitrust law without so much as a finding that it was perpetuated in good faith or was arguably lawful in compliance with the 1934 Act's reasonable rate standard. Under this approach, Exchange self-regulation over rates carries no accompanying duties to justify rates and rate structure. No scheme adopted by Congress which expressly provides for an antitrust immunity permits the immunity to arise independent of agency approval or action. Yet the immunity invoked below is based on nothing more than respondents' unjustified perpetuation of a rate-fixing scheme in obvious conflict with the antitrust laws. The immunity merely serves to congratulate respondents' commercial cunning. The approach thus adopted by the court below confers a blanket antitrust immunity to virtually everything done by the Exchange membership in the guise of self-regulation under Section 19(b) of the Exchange Act. That is the dangerous precedent this Court is asked to review.

C. The Approach Taken By The Court Below Invokes An Antitrust Immunity Without Finding That The S.E.C. is a Pervasive Regulatory Authority With Jurisdiction To Decide Antitrust Issues. The Decision Below Therefore Conflicts With the Philadelphia National Bank and the Federal Power Commission cases.

The decision below invoked an implied antitrust immunity without a concommitant finding that the S.E.C. is a pervasive regulatory authority over commission rates and structure, and over competitive factors with respect thereto, nor was a finding made that the S.E.C. has power to decide antitrust matters. This "approach" is in conflict with this Court's opinions in *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 351-352 (1963) and *California* v. *Federal Power Comm'n.,* 369 U.S. 482 (1962).

An issue in the instant case is the pervasiveness of the S.E.C.'s regulatory authority over Exchange-member rates and rate structure. The core need of that pervasiveness is the safeguard it provides against anticompetitive abuses (restraints of trade) adopted and perpetuated in the guise of rate self-regulation. Absent a check upon such abuses via pervasive regulatory safeguards, investors are entirely at the mercy of the respondents. NYSE-member commission law and practice offers a classic example of concentrated economic power and anticompetitive abuses unchecked by a pervasive regulatory authority and, as decided below, unchecked by the antitrust laws.

If, as the court below held, the antitrust laws were not applicable to respondents' rate-fixing agreement, in lieu of that safeguard it was imperative to find that the S.E.C. was a pervasive regulator over rates and rate structure. But, all the court below did was to state that "it is important to note" that the S.E.C. has power under

§19(b) of the Exchange Act to alter or supplement exchange rules in respect to the fixing of reasonable rates of commission (App. 10a). To what extent this provision comprises a pervasive regulatory scheme, if at all, the court below did not say.

There are two aspects to the issue of a pervasive regulatory authority, the statutory scheme itself, and how it operates in fact. The latter is especially important because the degree of S.E.C. involvement with rate structure is, after all, the measure of investor protection afforded by the agency as well as a reflection of the nature and extent of its self-considered rate regulatory duties.

Had the court below considered the issue of regulatory pervasiveness it would have been hard put to find it. As S.E.C. Chairman Cohen recently observed, "* * * Congress did not establish a comprehensive scheme of Federal Regulations in the Federal Securities laws, particularly in the economic sphere * * *" (Supp. Aff. Ex. 29, p. 1). The 1934 Act itself declares no economic policy and no competitive policy. The S.E.C. has discretion but no duty to review rates, approve rates or hold a rate hearing. The Act does not assign the S.E.C. a role of oversight over unfair methods of competitive or discriminatory practices, nor is it assigned broad remedial powers with respect thereto. If and when the S.E.C. reviews commission rates, there is no duty upon it to consider the factor of competitiveness or to give that factor any weight or to enforce any clearly delineated competitive standard. The oblique scheme of S.E.C. rate regulatory oversight prescribed by the Exchange Act is a model of vagueness and uncertainty. It bears no resemblance to the kind of scheme held pervasive in *Pan American World Airways* v. *United States,* 371 U.S. 296 (1962); *United States* v. *Philadelphia National Bank,* 374 U.S. 321, 351 (1963).

In only one area of S.E.C. jurisdiction is enforcement compliance involving an antitrust issue vested in the S.E.C. That involves approval of a merger of utilities under the Public Holding Company Act of 1935, 15 U.S.C. §79j. Section 7 of the Clayton Act, as amended, 15 U.S.C. §18 specifically excludes jurisdiction of the Federal Trade Commission over such mergers. Section 11 of the Clayton Act, 15 U.S.C. §21 (a) excludes Federal Trade Commission authority over transactions duly consummated pursuant to authority given to various regulatory agencies, but the S.E.C. is not among them. Yet even these exceptions to Federal Trade Commission jurisdiction do not constitute a grant of power "which it does not already possess" to adjudicate antitrust issues. *California* v. *Federal Power Commission*, 369 U.S. 482, 486-487, 490 (1962). Where, then, does the S.E.C. have jurisdiction to decide antitrust issues?

The overwhelming non-pervasiveness of the S.E.C.'s regulatory involvement, not merely with rates and rate structure but with all Exchange operations, occupies a major part of the Special Study. The court below did not cite a single instance where the S.E.C. exercised its §19(b) powers over rates, for the simple reason that the S.E.C. never has. The dangerous precedent established is that unused regulatory power, power guided by no clearly delineated competitive standard and direction, constitutes regulatory pervasiveness sufficient to invoke an antitrust immunity. If S.E.C. rate power is pervasive, the S.E.C. seems unconcerned about it. After 33 years and the NYSE's adoption of five rate increases (at minimum rates), the S.E.C. has never convened a rate hearing or instituted a formal rate investigation, nor has it ever required the NYSE to justify the basis upon which Exchange members collect well over $1 billion annually in

commissions at uniform, no discount rates coupled with the practice of reciprocal give-ups. Insofar as administrative review must be based upon a record, substantial evidence, findings and conclusions, no such review has ever been undertaken by the S.E.C. with respect to NYSE-member rates and rate structure. The rudiments of the administrative process have never begun to operate on commission rates and rate structure, much less operate pervasively. Without a definition of reasonable rates to begin with there could be no S.E.C. rate review; yet, so non-pervasive is the Exchange Act scheme that the S.E.C. has never conceived a duty under it to articulate a definition.

Between 1958 (the last year a rate increase was adopted) and 1966, the investing public has paid NYSE-members over $6 billion in commissions, pursuant to NYSE commission law. This fantastic sum is based on nothing more substantial than a superficial 15 page report filed by the NYSE with the S.E.C. in 1958 (the year of the last rate increase). (Appendix of Exhibits, Ex. 6) Cf. the voluminous 855 page record made by the Secretary of Agriculture in fixing *maximum* commission rates under a statutory standard of reasonable rates. *Tagg Bros. & Moorhead* v. *United States,* 280 U.S. 420 (1930), Oct. Term, 1929, No. 45, Transcript of Record, Vol. 1 & 11.

In 1965 the S.E.C. sought to enlist Congressional support to amend the Exchange Act so as to clearly delineate standards guiding S.E.C. rate review power and to expressly provide for judicial review of any failure by the S.E.C. "to give proper weight to antitrust considerations." (Supp. Aff. Ex. 23 and Ex. 29). Thus, while the S.E.C. itself recognized fatal deficiencies in the Exchange Act

scheme with respect to its regulatory role over antitrust issues, the court below did not.

The S.E.C.'s Investment Company Report in December, 1966, page 13, recommended amendment of the Investment Company Act of 1940 to provide that all compensation paid to mutual fund advisers be subject to the standard of reasonableness pursuant to detailed, delineated guidelines expressly including the competitive factor. The S.E.C. also recommended an amendment expressly allowing a remedy to recover damages for excessive compensation. *The very things lacking* in the Exchange Act scheme to confer pervasive regulatory oversight in the S.E.C. comprise amendments now urged by the S.E.C. with respect to enlarging its regulatory duties over the Investment Company Act. What the S.E.C. apparently now regards as essential to its having antitrust jurisdiction over management rates charged mutual funds by their investment advisers, the court below rejected *sub silentio* as inapposite to the S.E.C.'s antitrust jurisdiction over reasonable rates of commission. The respective views of the court below and the S.E.C. are irreconciliable. Clearly, the S.E.C. does not share the view of the court below that Section 19(b) of the Exchange Act confers pervasive regulatory power in the S.E.C. or power to decide antitrust issues.

III.

THE APPROACH TAKEN BY THE COURT BELOW IMPLIED AN INTENT BY CONGRESS TO AUTHORIZE EXCHANGES TO FIX UNIFORM MINIMUM RATES OF COMMISSION. THE HISTORY OF THE 1934 EXCHANGE ACT BELIES SUCH AN INTENT.

The decision below states: "(T)he district court found that the exchange's power to fix minimum rates existed

by implication." (App. 10a) But the basis for this implication (ostensibly adopted by the court below rests on a completely erroneous approach which nullifies the Exchange Act's standard of reasonable rates.

In support of the District Court's implication of Congressional intent to authorize exchanges to fix uniform rates, its opinion noted that Congress was well aware of defendant's commission law when it enacted the Exchange Act but did nothing to outlaw the long established practice (App. 5a). The fact remains that between passage of the Sherman Act in 1890 and the Exchange Act in 1934, defendants' rate fixing agreement (of services)[24] was unquestionably a violation of the Sherman Act. Long before 1934 opinions of this Court conclusively established the interstate character of brokerage businesses employing telegraph transmission lines.[25] By 1927 price fixing was a *per se* unreasonable restraint of trade. *United States* v. *Trenton Potteries,* 273 U.S. 392, 397-398.

The proper approach then is to determine whether Congress intended to grant Exchange members an ex-

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[24] *United States* v. *Trans-Missouri Freight Ass'n.,* 166 U.S. 290, 312 (1897); *United States* v. *Joint Traffic Ass'n.,* 171 U.S. 505 (1898); *Atlantic Cleaners & Dyers* v. *United States,* 286 U.S. 427 (1932); *Indiana Farmers Guide Pub. Co.* v. *Prairie Farmer Pub. Co.,* 293 U.S. 268 (1934); Cf. *United States* v. *Real Estate Boards,* 339 U.S. 485, 492 (1950).

[25] *Western Union Tel. Co.* v. *Foster,* 247 U.S. 105, 113-114 (1918); *Western Union Tel. Co.* v. *Speight,* 254 U.S. 17, 18 (1920); *Bedford Art Stone Co.* v. *Journeyman Stone Cutters Ass'n.,* 274 U.S. 37, 49. As early as 1918 the interstate character of grain brokerage operations was not an issue. *Board of Trade of the City of Chicago* v. *United States,* 246 U.S. 231 (1918).

emption from the antitrust laws. As S.E.C. Chairman Cohen has noted:

> "In the extensive legislative history which led up to the enactment of the Securities Exchange Act, we find no reference to the application of the antitrust laws." (Supp. Aff. Ex. 29)

Thus, although Congress was aware of the state of the antitrust laws, applicability to all rate fixing conspiracies when it debated adoption of the Exchange Act, the debates reveal no consideration of antitrust issues. If Congress intended to grant an immunity or to inaugurate a scheme providing for exchanges to legislate their own immunity or for the S.E.C. to grant such immunity, Congress would have at the very least debated the point. "The kind of conduct proscribed by the Sherman Act is simply not such that Congressional silence may be interpreted as congressional approval." *Pan American World Airways* v. *United States,* 371 U.S. 296 (1962), dissent, Mr. Justice Brennan, p. 324. *United States* v. *Trans-Missouri Freight Ass'n.,* 166 U.S. 290, 316 (1897). The Exchange Act not only fails to provide any express antitrust immunity to a rate-fixing agreement, but it expressly preserves all pre-existing rights and remedies. Section 28(a); 15 U.S.C. §78bb(a). Congress thus chose to preserve pre-existing antitrust rights and remedies, not to extinguish them. Nerenberg, *Applicability of the Antitrust Laws,* 16 W. Res. L. Rev. Vol. 16, p. 132, Ftn. 9 (1964).

Congress surely knew that uniform rates would eliminate rate competition. Neither the 1934 Act nor the debates reveal any such economic or other policy to be served via a restriction of competition. Congress could hardly have intended to restrict competition unless such

restriction served some overriding national policy. On the contrary, S.E.C. Chairman Cohen has noted that "It was not the purpose of the Exchange Act, unlike certain other regulatory statutes, to limit or restrict competition in the securities industry." (Supp. Aff. Ex. 23, 111 Cong. Rec. 18309, 18312) Chairman Cohen also stated that Congress intended to rely on competition as the best means of protecting the public. (Supp. Aff. Ex. 29). The district court's implication of Congressional intent to allow Exchange members to eliminate rate competition via uniform rates is contradicted by the absence of any purpose or policy of the Exchange Act to limit such competition.

A more direct clue to Congressional intent is to be found in the original bill (Section 18c) dealing with commission rates. This bill conferred direct regulatory authority in the (Federal Trade) Commission to "fix or prescribe the method of fixing *uniform* rates of commission." (emphasis added) H.R. 7852 and S. 2693, *Hearings on Stock Exchange Practices Before the Senate Committee on Banking and Currency,* 73rd Cong. 1st and 2nd Sess. p. 6432. The bill that passed, the present §19 (b); 15 U.S.C. §78s (b); deleted the word *uniform* and substituted "reasonable rates" as the rate standard. Other changes were made giving exchanges the right (duty?) to initiate and adopt reasonable rates subject to S.E.C. oversight. Between the first bill's §18(c) and the present § 19 (b), there were no debates reported regarding the change. The opinions of the courts below make no mention of this bit of legislative change. If Congress intended the exchanges to have the power to adopt uniform rates, why did it instead substitute therefore a standard of reasonable rates?

If there are doubts about whether uniform rates or competitive rates protect investors, the Maloney Amendment to the Exchange Act, passed in 1938, 15 U.S.C. §78o-3 has clarified Congressional intent. The Maloney Amendment expressly prohibits a registered association (of over-the-counter dealers) from fixing minimum rates of commission, "to provide safeguards against unreasonable profits or unreasonable rates." 15 U.S.C. §78o-3 (b)(8). Congress can hardly have intended the self-regulatory power of Exchange-members to adopt reasonable rates to carry a power to adopt minimum rates, in view of the positive Congressional recognition of the fact, albeit four years after passage of the Exchange Act, that only competitive rates provide investors with a safeguard against unreasonable rates.

IV.

THE APPROACH TAKEN BELOW IGNORED ESSENTIAL ECONOMIC DISTINCTIONS BETWEEN FIXED RATES APPLIED TO REGULATED UTILITY-TYPE BUSINESSES AND BROKERAGE OPERATIONS WHICH ARE OF IMPORTANCE IN THE REGULATORY FIELD.

Although not discussed in the decision below, the District Court's opinion construed the Exchange's power to fix reasonable rates of commission under Section 19(b) as "plain Congressional intent" authorizing the fixing of minimum rates of commission (App. 7a). In support of this "plain Congressional intent" the District Court relied upon an analogy whose faultiness refutes the very intent supposedly so "plain". The District Court stated "The requirement of 'reasonable' rates must accordingly be read in the sense employed in other statutes, where the charges of public utilities are directed to be regulated and fixed at 'reasonable rates'." Illustrating the point,

the District Court cited sections in the Communications Act of 1934, the Interstate Commerce Act and the Federal Aviation Act. (App. 7a).[26]

In citing "reasonable rates" administered by these other agencies, the District Court fashioned the contradiction of its own "approach"; for it failed to make essential distinctions between utility-type operations characterized by a high fixed asset base and a common cost and profit experience, and brokerage operations characterized by a labor base and a diversity of cost and profit experience. A reasonable rate applied to utility-type businesses produces a profit which can be geared to the asset base as a rate of return, all of which has intrinsic economic rationality and validity. Moreover, among competing utility-type businesses there is a similarity of cost and profit experience so that a fixed rate produces a similarity of profits within a narrow range. But the brokerage operation involves a labor base rather than an asset base; a reasonable rate necessarily embraces a reasonable return on labor.

The consummate economic invalidity of uniform rates being reasonable rates lies in the enormous diversity of profits among NYSE member firms, although they all charge fixed rates. A tally of the 177 largest NYSE firms included in NYSE surveys between 1961-1964 reveals that

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[26] The regulatory schemes alleged are very much different from the Exchange Act scheme, with respect to special economic and competitive policies incorporated therein, the pervasiveness of agency rate review and express remedies provided for rate overcharges. The Communications Act, 47 U.S.C. §205 authorizes the Commission to fix reasonable charges, maximum or minimum or maximum and minimum charges. A similar authority is given under the Interstate Commerce Act, 49 U.S.C. §316 (e) and under the Federal Aviation Act, 49 U.S.C. §1482.

seven had profits exceeding 30% (of gross commission income), fourteen had profits between 20-30%, thirty-nine had profits between 19-20%, twenty-seven had profits under 10%, and forty experienced losses. (Counteraff. 46b). Each brokerage house is a separate economic entity with its own cost and profit experience. On no basis in logic, economics or law can it be argued that fixed rates are reasonable when they yield profits of over 40% to some brokers, losses exceeding 5% to others and an infinite number of yields in between. The effect of minimum rates rewards "efficient" brokers with unconscionable profits while subsidizing inefficient, incompetent brokers. It is apparent, then, that the fixed rate concept applied to brokerage operations is merely an artificial pricing mechanism which has no economic relationship to any common denominator of reasonable rates. Thus it is that neither the NYSE nor the S.E.C. has ever been able to articulate a definition of reasonable rates or to identify a particular percentage of profits, or range of percentages, or any other quantitative standard as a measure of fair return or of the reasonableness of a particular rate schedule. (Special Study, Part 2, page 337; Counteraff. 40).

The "approach" thus adopted by the District Court, and approved by the court below, in affirming Congressional intent to allowing exchanges to adopt minimum rates as reasonable rates is completely disaffirmed by an analysis of the economics of brokerage operations, an analysis the District Court failed to make from facts in the record. If uniform rates produce no coherent uniformity of profits, but result instead in unreasonable and unconscionable profits, on what basis can it be said that such rates are reasonable? Congress could not have intended exchanges to have the power to adopt rates and rate structure inherently unreasonable and in direct contradiction to its own standard that they be reasonable.

V.

PETITIONERS HAVE NO EFFECTIVE REMEDY EXCEPT UNDER THE ANTITRUST LAWS.

An anomaly of the 1934 Act is that investors must turn to the antitrust laws for a remedy to fulfill Exchange Act purposes to protect investors against unreasonable rates of commission. The 1934 Act contains neither an express nor an implied remedy allowing investors to recover damages sustained as a result of unreasonable rates and rate structure. Cf. *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1963). Nor does the Act confer power in the S.E.C. to order damages refunds or reparations, past, present or future. Unless investors are protected with a damages remedy under the antitrust laws, the defendants are free to retain the multi-million dollar benefits flowing from commission law and its interlocking assortment of unreasonable restraints of trade. That Congress intended the 1934 Act scheme to confer such a total dispensation (via a complete immunity to damages) suggests a solicitude for NYSE brokers not corroborated in the debates leading up to passage of the Act. Yet that is the effect of the decision below. If it is correct, investors would be better off, rate-wise, if the 1934 Act had never been passed. For in such case the antitrust laws would surely apply to respondents' commission law, both to restrain it and to allow damages to persons injured by it. Congress can hardly be supposed to have intended, in passing the 1934 Act, to extinguish the only remedy available to investors to collect their damages, and to extinguish the only effective check against otherwise unchecked Exchange-member economic self-interest. Whatever the S.E.C.'s rate regulatory powers encompass under §19(b), they do not include the power to award damages. Cf.

Keogh v. *Chicago C.W. Ry. Co.*, 260 U.S. 156, 162 (1922); *United States* v. *Morgan*, 307 U.S. 193, 190 (1939). The fact that Congress failed to provide the S.E.C. with pervasive remedial powers to order damage reparations is another aspect of the incomplete and ineffective bond of protection afforded investors under the 1934 Act scheme. Cf. *Atlantic Refining Co.* v. *Public Service Comm'n. of N.Y.*, 360 U.S. 357, 388-389 (1959). The absence of an investor remedy to recover damages under the 1934 Exchange Act scheme (affirmed by the trial court's dismissal of such claims asserted in petitioners' amended complaint) serves to emphasize the need to apply damages sanctions provided by the antitrust laws. Sections 4 and 16 of the Clayton Act; 15 U.S.C. §15 and §26.

The *Silver* case, *supra*, turned in part on Silver not having a remedy of S.E.C. review with respect to an application of Exchange rules resulting in a group boycott against him. In the case at bar the essence of unreasonable rates consists of continuing rate overcharges, and the only remedial check appropriate to repair such injury is damages. Such damages are recoverable only under the antitrust laws.

Under the erroneous approach taken by the courts below, the vehicle of S.E.C. rate review under §19(b) was sufficient to invoke an implied repeal, without even considering the fact that such review did not comprehend remedial powers, especially powers to award damages. Yet these broad remedial powers were identified by this Court as part of the package of ingredients essential to an implied repeal. *United States* v. *Philadelphia National Bank*, 374 U.S. 321, 351 (1963).

But even apart from the recovery of damages, investors have no remedy under the 1934 Exchange Act to initiate

a rate contest, or to compel the S.E.C. to invoke a rate hearing. By the simple expediency of the S.E.C.'s never having convened a rate hearing there has never been a concluded rate proceeding under the 1934 Exchange Act subject to judicial review.

The Federal Administrative Procedure Act, 5 U.S.C. §1001 *et seq.* does not provide investors with an effective remedy to trade at reasonable rates, and there is no provision under that Act authorizing investors to invoke a remedy of damages for rate overcharges. Section 1003(d) provides that every agency shall accord any interested person the right to petition for the issuance, amendment or repeal of a rule, but there is no duty upon the S.E.C. to act upon such petition. The only other possible action under the Act would be judicial review of the S.E.C.'s agency action in failing to act with respect to conducting a rate proceeding for the purpose of defining, determining and approving reasonable rates, 5 U.S.C. §§ 1001(c); 1001(g); 1009(a). But the entire right to judicial review of the S.E.C.'s failure to act depends upon whether S.E.C. rate action is by law committed to agency discretion, 5 U.S.C. §1009, and under Section 19 (b) of the 1934 Exchange Act it is discretionary with the S.E.C. to request an exchange to adopt rules with respect to reasonable rates of commission. Thus, the Administrative Procedure Act provides no effective remedy to compel the S.E.C. to review and implement reasonable rates.

CONCLUSION

A major component of national wealth consists of stocks traded on the New York Stock Exchange. It is vital to national economic health that the primary market for the trading of those stocks be free from anticompeti-

tive restraints which serve no demonstrable overriding public purpose. Exchange rules prescribing fixed, no-discount rates of commission exact from the institutions represented by petitioners arbitrary, unreasonable and unjustified rates of commission. Only the antitrust laws provide petitioners with meaningful relief to compel the respondents to provide a market that is free, competitive and viable. That the New York Stock Exchange, as the epitome of free-enterprise should itself be the focal point for grand-scale restraints of trade, is an anomaly of our time. This Court is here presented with consideration of the novel question of whether the public shall continue to be arbitrarily subject to respondents commission law without a remedy, or whether the antitrust laws shall be deemed to apply so as to bring respondents into the mainstream of American competitive life. This question commends itself to a determination by this Court.

Respectfully submitted,

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APPENDIX

Memorandum and Order of the United States District Court, February 25, 1966.

Julius J. Hoffman, District Judge. A seeming conflict between the federal antitrust laws and the Securities Exchange Act of 1934 is the source of this controversy. The reconciliation of these apparently opposing policies is a matter of considerable moment to the financial community and to the investing public. The point at issue is the legality of the practices of stock exchanges in fixing minimum rates for the commissions charged by stock exchange members for the purchase and sale of securities on the exchange.

The action was brought by the plaintiff Kaplan and by the plaintiff Dunn (on behalf of her minor children) as a shareholder's derivative suit and at the same time as a representative class action. The plaintiffs thus purport to sue on behalf of, and in the right of, some five corporations which are qualified as investment companies and which are generally known in the financial world as mutual funds, and to sue on behalf of their shareholders as a class. These five mutual funds are joined as nominal defendants, and include One William Street Fund, Inc., The Lehman Corporation, Energy Fund, Inc., The Dominick Fund, Inc., and The Chemical Fund.

The actual defendants ar the New York Stock Exchange (hereafter referred to as the Exchange) and four member firms of that exchange: Lehman Brothers, Goodbody & Co., Dominick & Dominick; Incorporated, and Paine, Webber, Jackson & Curtis. These firms, with others, it is alleged, act as brokers and agents for the

mutual funds in the purchase and sale of stocks listed on the Exchange. Jurisdiction is based upon the antitrust laws, the Securities Exchange Act of 1934, and Sections 1331 and 1337 of the Judicial Code, 28 U.S.C. §§1331, 1337.

The gist of the complaint is the allegation that "Since the year 1792 and up to the present time, an avowed purpose of the defendant (Exchange) has been to set and fix minimum rates of commission to be charged to the public by its members . . . on all brokerage transactions executed on the" Exchange. The constitution of the Exchange thus specifies the exact schedule of minimum commissions to be charged, and pledges all members to obedience. The Exchange polices these rates, and members who violate them are subject to expulsion. Claiming that this arrangement amounts to a combination and conspiracy in restraint of trade in violation of Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 et seq, and that the mutual funds have been damaged thereby in an amount equal to the difference between commission rates which have been charged under the Exchange rules and the rates that would have been available to the mutual funds "by operation of free and open competition had no such contract, combination and conspiracy existed," a demand for judgment for three times those damages is made under the antitrust laws, and, in the same count and upon the same factual allegations, a demand for judgment for the actual damages, unmultipled, is presented on the theory that the alleged misconduct also offends against the Securities Exchange Act of 1934. Still in the same count, the complaint prays for a declaratory judgment holding the rules of the Exchange to be null and void insofar as they prescribe minimum rates of commission, and declaring that all Exchange

members are individually free to determine and set their own rates of commission.

The defendant Exchange and its member firms named as defendants have joined in a motion for summary judgment or, alternatively, to dismiss the complaint for failure to state a claim upon which relief can be granted. The parties have presented voluminous affidavits and exhibits outside the pleadings, and the Court is thereby constrained to treat the motion solely as a motion for summary judgment. Rule 12(c), Fed. R. Civ. Pro.

The opposing briefs disclose no significant disagreements between the opposing sides on the factual basis of the controversy. The affidavits present no genuine issue of material fact to be tried.

The sole question is a matter of law, appropriate for disposition on a motion for summary judgment.

I.

It is undisputed that the Exchange, by vote of its membership, has fixed the rates of commission to be charged by its members, and that those members have agreed to, and do, abide by those rates. Whether the antitrust laws forbid such price-fixing turns upon the interpretation of the Securities Exchange Act of 1934. The parties are agreed on the authoritative source of the principles which control the reconciliation of the Sherman Act and the Securities Exchange Act: the pronouncements of the Supreme Court in Silver v. New York Stock Exchange, 373 U.S. 341 (1963). They part company on the application of those principles to the case at hand.

In Silver, the plaintiff was a broker and dealer in securities but not a member of the Exchange. He made

arrangements with certain Exchange members for direct-wire connections with their offices, to provide him with quotations and other information essential to his business. Under the rules of the Exchange, such direct-wire connections between members and non-members require approval by the Exchange. After tentative and temporary approval, the Exchange denied permission and the connections were severed without giving notice or reasons and without affording plaintiff an opportunity to be heard. His suit for trebles damages under the antitrust laws was sustained by the Supreme Court.

At the outset, the Court concluded that the Exchange was empowered to make rules on the subject of its members' connections with non-members, in order to exclude "bucket shops", "boiler shops", and similar operations. Under the statutory scheme of the Securities Exchange Act of 1934, the various exchanges are obliged to regulate themselves, subject to the surveillance of the SEC, in the interests of stability in the securities market. The exchange, in this process of self-regulation, is obliged to have rules which are "just and adequate to insure fair dealing and to protect investors." Section 6(d), 15 U.S.C. § 78f(d). Registration may be granted to the exchange only if its rules provide "for the expulsion of a member for conduct or proceedings inconsistent with just and equitable principles of trade." Section 6(b). These broad declarations sufficed to validate exchange rules requiring approval of direct-wire connections, the court concluded.

This conclusion led to the collision of policy. "It is plain, to begin with," wrote Mr. Justice Goldberg for the majority, "that removal of the wires by collective action of the Exchange and its members [illegible], had it occurred in a context free from other federal regu-

lations, constitute a per se violation of § 1 of the Sherman Act." 373 U.S., at 347. In this circumstance, the Court unanimously concluded that such conduct could not constitute a violation, in and of itself, of the antitrust laws. In other words, the decision makes it plain that action taken by the Exchange and its members, pursuant to its statutory authority to make rules, is not illegal per se under the Sherman Act.

This basic conclusion served only as a beginning in the Silver case, in view of the remaining questions raised by its facts. It is the final conclusion here. The plaintiffs have cast their lot entirely upon their proposition that the fixing of minimum rates of commission through the collective action of the Exchange is illegal per se under the Sherman Act. If such action is within the authority conferred upon the Exchange by the Act of 1934, however, the direct precedent of the Silver decision stands squarely against them.

Since 1792, when the Exchange was founded with the so-called Buttonwood Tree Agreement, the rules of the Exchange have set minimum rates for the commissions to be charged by its members for buying or selling stocks upon the Exchange. These rules were not called into question after the adoption of the Sherman Act. In the legislative deliberations which preceded the enactment of the Securities Exchange Act of 1934, the existence of such rules was plainly in evidence and duly noted. No action was taken to outlaw the long-established practice. The securities exchange, although not a free and open market, served a public purpose by assuring investors of ready liquidation of their holdings and by affording a ready source of capital for business and industry. Congress thus chose to preserve the benefits of the exchanges, and

to eliminate practices which, by undermining public confidence, might impair those beneficial functions.

The legislative means chosen to achieve these ends left the original regulating power in the exchange itself, and relied upon the SEC as the overseer empowered to protect the public interest. The Exchange was entitled to registration under the Act only if it had adopted rules which were required to be submitted to, and approved by, the SEC.

The SEC is then authorized to "alter or supplement" those rules if, after request, the exchange fails to effect specified changes on its own. Section 19(b) of the Act, 15 U.S.C. § 78s. In that section, Congress enumerated twelve subjects of the exchange's rulemaking power to which the SEC's power to alter or supplement would extend, including the listing of securities, hours of trading, the reporting of transactions, and "similar matters." Listed ninth among these matters for exchange rules is "(9) the fixing of reasonable rates of commission, interest, listing, and other charges." Section 19(b)(9), 15 U.S.C. § 78s.

It may be conceded that the rulemaking power thus conferred is granted in a manner which is somewhat oblique. No simple declarative sentence vests the exchange with power to fix minimum rates. Yet the power is recognized by the plainest implication. The SEC's authority to request changes in rules concerning "the fixing of reasonable rates" necessarily presupposes rules of the Exchange on that subject. If none were adopted by an exchange, the SEC could "supplement" them, after due request.

The plaintiffs seeks to support their per se attack, in the face of this Congressional sanction for rate-fixing,

by emphasizing the requirement that rates of commission must be "reasonable." Prescribed minimum rates, they assert, can never be "reasonable"; only free competitive rates comport with reason. The argument imputes a contradiction which would confound the plain Congressional intent, since it ignores the provision that the "reasonable" rates shall also be "fixed" rates. The requirement of "reasonable" rates must accordingly be read in the sense employed in other statutes, where the charges of public utilities are directed to be regulated and fixed at "reasonable rates." E.g., Communications Act of 1934, 47 U.S.C. § 201; Interstate Commerce Act, 49 U.S.C. §§ 1(4), 1(5), 316; Federal Aviation Act of 1958, 49 U.S.C. § 1374.

Since the plaintiffs have attacked the legality of the Exchange rules and their prescribed rates of commission solely on the ground that fixed rates are illegal, the holding in Silver v. New York Stock Exchange, 373 U.S. 341 (1963) is a complete bar to their claim. Rules adopted by an Exchange under the authority of the Act are not illegal per se.

In the Silver case, the Supreme Court went on, after holding the rules not illegal per se, to consider the remaining questions in the case. Since the power to sever wire connections with non-members could be used to eliminate competition by such a non-member as well as to serve the purposes of securities regulations by excluding unethical or irresponsible dealers, the Court conferred the right upon the non-member to a review of the justification for the termination of the direct-wire connections essential to his business. Finding that nothing in the Securities Exchange Act of 1934 gave the SEC the power to review particular adjudicative decisions of the Exchange in enforcing and applying its rules, and distinguished from review of the legislative action in-

volved in making such rules, the Court concluded that the remedy of review must be found in the judicial branch. Since the misuse of the power to sever wire connections to injure a non-member competitor would not serve the purposes of securities regulations, there remained no policy of securities control to exclude the application of the antitrust laws or to immunize the conduct. Since the Exchange had refused to give notice or reasons or to afford a hearing to determine the justification for its action as an appropriate measure to protect the investing public, the plaintiff prevailed.

This holding adds nothing to the claim of these plaintiffs. The power to deny information to non-members of an exchange is plainly susceptible to misuse as a means to destroy competition. The power to fix rates, unlike the power to exclude, is not a weapon that can be used to injure a particular competitor. The rates, once fixed, apply equally to all Exchange members and to all customers. It is not suggested by the plaintiffs here that the rates are not uniformly applied, that the schedules are discriminatory, or that the power has been used to eliminate competition beyond that elimination inherent in any system of authorized price-fixing.

Moreover, this aspect of the Silver decision is expressly predicted upon the absence of SEC power to review the particular action. "Should review of exchange self-regulations be provided through a vehicle other than the antitrust laws, a different case as to antitrust exemption would be presented." (373 U.S., at 360). This is the "different case", since the SEC exercises a general and continuing power to change, alter, or supplement the rules of the Exchange fixing the rates of commission. Since review is afforded within the system of securities regu-

lation, there is no need to resort to the antitrust laws for a remedy.

The plaintiffs have complained of the rates because they are fixed. If they had complained instead that the rates were too high, they would find no support in the antitrust laws. The remedy for a level of rates that is unreasonably high rests with the SEC. Ratemaking is a matter for which the courts are ill-equipped, and accordingly a matter traditionally committed to an administrative agency. See Board of Trade of Kansas City v. United States, 314 U.S. 534, 546 (1942). The SEC since its establishment has exercised this power of review over Exchange rates of commission, and it has inaugurated a regular system of reporting from Exchange members to furnish the necessary information.

To subject the Exchange to the perils of treble liability, retroactively imposed, upon the variant decisions of different courts in determining the reasonableness of rates would inevitably disrupt the congressional plan designed to bring order to the marketing of securities. To leave the determination of reasonableness to the prospective decisions of the agency which is especially qualified and responsible for the general supervision of the industry will assure the intention of Congress as well as the interests of the public.

Judgment will be entered, accordingly, for the defendants' with costs to be assessed against the plaintiffs.

Opinion of the United States Court of Appeals for the Seventh Circuit. January 4, 1967.

Before SCHNACKENBERG, CASTLE and FAIRCHILD, *Circuit Judges.*

SCHNACKENBERG, *Circuit Judge.*

Plaintiff Harold Z. Kaplan, and minor plaintiffs Frederick L. Dunn, Daniel B. Dunn, Charlotte F. Dunn and Nancy L. Dunn, by Lila Dunn, their next friend, as shareholders in several named mutual funds, brought a class action derivatively for and on behalf of all shareholders of The Lehman Corporation, a Delaware corporation, and four other mutual funds.[1] An appeal on behalf of said plaintiffs was taken from a summary judgment of the district court in favor of defendants, New York Stock Exchange and four brokerage firms which are member firms in said exchange.[2]

Plaintiffs' amended complaint seeks recovery of treble damages against defendants for allegedly engaging in a coercive conspiracy fixing minimum uniform rates of brokerage commission and adhering to said rates in violation of the Sherman Antitrust Act.[3]

It is the theory of plaintiffs that the Securities and Exchange Act of 1934, 15 U.S.C.A. § 78a, et seq. contains no express grant of immunity from the antitrust laws for such alleged activities and neither does that act impliedly immunize or exempt the "minimum rate fixing activities" of the exchange from the antitrust laws. Plaintiffs rely on the language of § 19(b) of the act, 15 U.S.C.A. § 78s, but it is important to note that subparagraph (b) thereof does authorize the Commission to

> "* * * alter or supplement the rules of such exchange * * * in respect of such matters as * * *

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[1] Lehman Brothers, Goodbody & Co., Dominick & Dominick, Incorporated, and Paine, Webber, Jackson & Curtis.

[3] Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1 et seq.

(9) the fixing of reasonable rates of commission, * * *".

The district court found that the exchange's power to fix minimum rates existed by implication.

[1] With the aid of the exhaustive decision of the Supreme Court and Mr. Justice Stewart's dissenting opinion, in Silver v. New York Stock Exchange, 373 U.S. 341, 83 S.Ct. 1246, 10 L.Ed.2d 389 (1963), we are now able to determine that, although the "Securities Exchange Act contains no express exemption from the antitrust laws," a "repeal" thereof is to be regarded as implied "if necessary to make the Securities Exchange Act work". We accordingly interpret the district court's action as holding that the antitrust laws are inapplicable to the New York Stock Exchange insofar as its prescribing of minimum commission rates is concerned.

We further hold that in this situation the self-regulatory function of the exchange has been exercised by virtue of § 19(b).

[2] On the facts set forth in the complaint herein, we do not construe the Sherman act and the exchange act as showing a congressional intention to permit the maintenance of an antitrust prosecution of the exchange or its members to be based upon its action relating to rates of commission to be charged by its members. Obviously the fixing of minimum commissions is one method of regulating commission rates.

For the reasons herein stated, the judgment from which plaintiffs appeal is affirmed.

Judgment affirmed.

Order of the United States Court of Appeals for the Seventh Circuit. January 4, 1967.

This cause coming on to be heard on the transcript of record from the United States District for the Northern District of Illinois, Eastern Division, and was argued by counsel.

Upon consideration whereof, it is ordered and adjudged by this Court that said judgment of said District Court in this cause appealed be, and the same is hereby affirmed with costs in accordance with the opinion of this Court filed this day.

STATUTES INVOLVED

Section 1 of the Sherman Anti-Trust Act (15 U.S.C. § 1) reads as follows:

> "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal; Provided, That nothing contained in sections 1-7 of this title shall render illegal, contracts or agreements prescribing minimum prices for the resale of a commodity which bears, or the label or container of which bears, the trademark, brand or name of the producer or distributor of such commodity and which is in free and open competition with commodities of the same general class produced or distributed by others, when contracts or agreements of that description are lawful as applied to intrastate transactions, under any statute, law, or public policy now or hereafter in effect in any State, Territory, or the District of Columbia in which such resale is to be made or to which the commodity is to be transported for such resale, and the making of such contracts or agreements shall not be an unfair method of competition under section 45 of this title: Provided further, That the preceding proviso shall not make lawful any contract or agreement, pro-

viding for the establishment or maintenance of minimum resale prices on any commodity herein involved, between manufacturers, or between producers, or between wholesalers, or between brokers, or between factors, or between retailers, or between persons, firms, or corporations in competition with each other. Every person who shall make any contract or engage in any combination or conspiracy declared by sections 1-7 of this title to be illegal shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding fifty thousand dollars, or by imprisonment not exceeding one year or by both said punishments, in the discretion of the court."

Section 2 of the Clayton Act (15 U.S.C. § 15) reads as follows:

"Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendants resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee."

Section 16 of the Clayton Act (15 U.S.C. § 26) reads as follows:

"Any person, firm, corporation, or association shall be entitled to sue for and have injunctive relief, in any court of the United States having jurisdiction over the parties, against threatened loss or damage by a violation of the antitrust laws, including sections 13, 14, 18 and 19 of this title, when and under the same conditions and principles as injunctive relief against threatened conduct that will cause loss or damage is granted by courts of equity, under the rules governing such proceedings, and upon the execution of proper bond against damages

for an injunction improvidently granted and a showing that the danger of irreparable loss or damage is immediate, a preliminary injunction may issue: * * *."

Section 2 of the Securities Exchange Act of 1934 (15 U.S.C. § 78 b)

"For the reasons hereinafter enumerated, transactions in securities as commonly conducted upon securities exchanges and over-the-counter markets are affected with a national public interest which makes it necessary to provide for regulation and control of such transactions and of practices and matters related thereto, including transactions by officers, directors, and principal security holders, to require appropriate reports, and to impose requirements necessary to make such regulation and control reasonable complete and effective, in order to protect interstate commerce, the national credit, the Federal taxing power, to protect and make more effective the national banking system and Federal Reserve System, and to insure the maintenance of fair and honest markets in such transactions:

(1) Such transactions (a) are carried on in large volume by the public generally and in large part originate outside the States in which the exchanges and over-the-counter markets are located and/or are effected by means of the mails and instrumentalities of interstate commerce; (b) constitute an important part of current interstate commerce; (c) involve in large part the securities of issuers engaged in interstate commerce; (d) involve the use of credit, directly affect the financing of trade, industry, and transportation in interstate commerce, and directly affect and influence the volume of interstate commerce; and affect the national credit.

(2) The prices established and offered in such transactions are generally disseminated and quoted throughout the United States and foreign

countries and constitute a basis for determining and establishing the prices at which securities are bought and sold, the amount of certain taxes owing to the United States and to the several States by owners, buyers, and sellers of securities, and the value of collateral for bank loans.

(3) Frequently the prices of securities on such exchanges and markets are susceptible to manipulation and control, and the dissemination of such prices gives rise to excessive speculation, resulting in sudden and unreasonable fluctuations in the prices of securities and which (a) cause alternately unreasonable expansion and unreasonable contraction of the volume of credit available for trade, transportation, and industry in interstate commerce, (b) hinder the proper appraisal of the value of securities and thus prevent a fair calculation of taxes owing to the United States and to the several States by owners, buyers, and sellers of securities, and (c) prevent the fair valuation of collateral for bank loans and/or obstruct the effective operation of the national banking system and Federal Reserve System.

(4) National emergencies, which produce widespread unemployment and the dislocation of trade, transportation, and industry, and which burden interstate commerce and adversely affect the general welfare, are precipitated, intensified and prolonged by manipulation and sudden and unreasonable fluctuations of security prices and by excessive speculation on such exchanges and markets, and to meet such emergencies the Federal Government is put to such great expense as to burden national credit."

Section 6(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78f(b))

"(b) No registration shall be granted or remain in force unless the rules of the exchange include pro-

vision for the expulsion, suspension, or disciplining of a member for conduct or proceeding inconsistent with just and equitable principles of trade, and declare that the willful violation of any provisions of this chapter or any rule or regulation thereunder shall be considered conduct or proceeding inconsistent with just and equitable principles of trade."

Section 6 (d) of the Securities Exchange Act of 1934 (15 U.S.C. §78f(d))

"(d) If it appears to the Commission that the exchange applying for registration is so organized as to be able to comply with the provisions of this chapter and the rules and regulations thereunder and that the rules of the exchange are just and adequate to insure fair dealing and to protect investors, the Commission shall cause such exchange to be registered as a national securities exchange."

Section 15A as amended of the Securities Exchange Act of 1934 (15 U.S.C. 78o-3(b)(8))

"(b) An applicant association shall not be registered as a national securities association unless it appears to the Commission that • • •

(8) the rules of the association are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to provide safeguards against unreasonable profits or unreasonable rates of commissions or other charges, and, in general, to protect investors and the public interest, and to remove impediments and to perfect the mechanism of a free and open market; and are not designed to permit unfair discrimination between customers or issuers; or brokers or dealers, to fix minimum profits, to impose any schedule of prices, or to impose any schedule or fix minimum rates of commissions, allowances, discounts, or other charges."

Section 19 (b) of the Securities Exchange Act of 1934 (U.S.C. § 78 s(b))

"(b) The Commission is further authorized, if after making appropriate request in writing to a national securities exchange that such exchange effect on its own behalf specified changes in its rules and practices, and after appropriate notice and opportunity for hearing, the Commission determines that such exchange has not made the changes so requested, and that such changes are necessary or appropriate for the protection of investors or to insure fair dealing in securities traded in upon such exchange or to insure fair administration of such exchange, by rules or regulations or by order to alter or supplement the rules of such exchange (insofar as necessary or appropriate to effect such changes) in respect of such matters as * * * *

(9) the fixing of reasonable rates of commission, interest, listing, and other charges;"